The MORTGAGE BANKER

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THE DETROIT CONVENTION

By GEORGE H. PATTERSON

MBA's 26th annual Convention in Detroit was the third largest the Association has held and judging from comments made at the meeting and those contained in letters it was one of the most successful. Registration was 808, which has only been exceeded in the past by the two Chicago Conventions in 1934 and 1938 when attendance was 1007 and 1217 respectively. When MBA last met in Detroit in 1930, registration was 402, slightly less than half what it was this year.

Of those attending, 436 were from out of town and only 45 were non-member guests. This indicates, I believe, that members approve of the policy, tried out for the first time this year, of placing some limitation on attendance. It also clearly shows that our annual meeting can be made a success when such limitation is in effect.

There were 89 cities and 33 states represented at Detroit. Most of our insurance company and institutional lender members were represented as well as their correspondents. In addition, the government agencies with which our members are most directly concerned, had representatives at the Convention.

It seems to be generally agreed that the Detroit Mortgage Bankers Association and its Convention group headed by Charles H. Sill did one of the most effective jobs of staging a convention even seen in our Association. The entertainment features were singled out for particular praise.

The reception committee, headed by Walter Gehrke, functioned like clockwork and was a most efficient group. Another group coming in for much comment was the entertainment committee headed by Lloyd N. Wheeler and R. B. Hassett. The entertainment features were all that anyone could possibly ask for and letters coming to the headquarters office emphasize this point. Likewise, the golf committee succeeded in arranging and staging a tournament that pleased everyone. Some of the other committees whose work was handled just as efficiently but the results of which were probably not so conspicuous to those attending the Convention were: the registration committee headed by Herold G. Woodruff, the exhibit committee headed by Frank Kennedy, the finance committee headed by Donal Jenkins, and the publicity committee headed by Colonel Henry H. Burdick. The transportation committee headed by Earl K. Akey got and deserved many thanks from out-of-town delegates because of the interesting Ford Tours and other services. And while the compliments were passed around, there were plenty for Charles H. Sill, Walter J. L. Ray, Edward F. Lambrecht, and Louis H. Charbonneau.

The man who headed the Detroit convention group and the man who heads MBA for the coming year: Chas. H. Sill and Byron T. Shutz

Some of those who attended probably did not learn just who won the different golf and exposition prizes. The President's Cup this year was won by J. A. Grow, Jr., of Homer Warren and Company of Detroit. His score was 83. S. T. Crossland of Chicago and W. T. ZurSchmiede of Detroit had scores of 76 and 79 but they are non-members. Last year Earl E. Shipley of the Lincoln National Life Insurance Company branch in Chicago won the Cup, which was donated by Past President Owen M. Murray of Dallas.

Oscar Onstad of the Standard Accident Insurance of Detroit had first low net and R. M. Christian of the Life Insurance Company of Virginia branch in Chicago had second low net. Low score on blind holes was made by Fred E. Law of Chicago and high score on blind holes by N. T. Baskin.

More than seventy attended the tournament of which sixty were from out of town. The affair was arranged by a very efficient committee headed by Fred J. Beyer, vice president of The Manufacturers National Bank of Detroit.

Ira L. McKennie of The Franklin Life Insurance Company of Springfield, Ill., won the $100 first prize at the Exposition drawing. Last year Mrs. McKennie won third prize of $35. Alf Peterson, vice president of the Security State Bank of Madison, Wis., won second prize this year of $25 and a similar prize last year. Third prize went to Capt. D. C. Grattan of the RFC in Detroit and fourth prize to Arthur W. Carlson, vice president, Sutherland-Carlson Co. of Minneapolis.

FIVE NEW MEMBERS ELECTED TO MBA BOARD REPRESENTING EAST, SOUTHWEST AND MIDWEST

Byron T. Shutz, executive vice president of Herbert V. Jones & Co. of Kansas City, was unanimously elected president of the Mortgage Bankers Association of America at the Detroit Convention and Dean R. Hill, president of the Hill Mortgage Corporation of Buffalo, New York, was elected vice president for the 1939-1940 term. Five new board members were elected, the largest number to take seats on MBA's governing body at one time than ever before. The new governors are G. H. Galbreath of Tulsa, for a term expiring in 1942; and McCune Gill of St. Louis, Hugo Porth of Milwaukee, C. Armel Nutter of Camden, N. J., and Allyn R. Cline of Houston, all for terms expiring in 1943. Hence our newest governors come from the Southwest, Middle West and East.

G. H. GALBREATH

In addition, present board member J. P. Hogan of New Orleans was reelected for a term expiring in 1941 and board members R. O. Deming, Jr., of Oswego, Kan., C. W. Mead of Omaha, and Claude A. Campbell of Toledo were reelected for terms expiring in 1943.

All of the new board members are well known to the MBA membership.

G. H. GALBREATH OF TULSA

G. H. Galbreath is a native of Ohio, went to school at Mt. Sterling in that state and later attended Ohio University at Athens. He moved to Oklahoma in 1912 and to Tulsa in 1918. He has lived in Oklahoma since that time except for the period from 1924 to 1930, when he was in business in Columbus, Ohio.

He was formerly associated with the Exchange Trust Company of Tulsa for seven years and in 1933 organized the G. H. Galbreath Company, representing the investment accounts of three eastern insurance companies in Eastern Oklahoma and Tulsa. He served as president of the Tulsa Real Estate Board in 1937 and was one of the organizers and first president of the Tulsa Institute of Governmental Research. Last year he was president of the Oklahoma Mortgage Association. He has been a member of MBA since 1933.

McCUNE GILL OF ST. LOUIS

McCune Gill is vice president of the Title Insurance Corporation of St. Louis. Members will recall that he was a recent contributor to *The Mortgage Banker* with an article in the August 1st issue on "Helping Mortgage Bankers Over a Hurdle in Making Construction Loans."

McCUNE GILL

He is a past president of the American Title Association and is the author of various books on title law, among them "Gill on Missouri Real Estate Forms" and "Gill on Missouri Titles." He is a graduate of Washington University Law School and has spent his entire business life in practical and legal phases of title examination and escrow service.

His organization in St. Louis has an authorized capital of $1,000,000 and is one of the Middle West's leading title companies. He has been a member of MBA since 1930.

HUGO PORTH

HUGO PORTH OF MILWAUKEE

Hugo Porth is a native of Milwaukee and went from high school to an industrial firm, where he remained until 1917. He then joined his father, Ed Porth, and brother, Monroe Porth, in their mortgage and real estate firm. The senior Mr. Porth had originally entered the real estate field in 1884 as an office boy and later established his own organization in 1914. Ed Porth & Sons is still a three-way partnership.

Hugo Porth has been active in the National Association of Real Estate Boards. He is a past president of the Milwaukee Real Estate Board and the Wisconsin state organization. He is at present a regional vice president of the NAREB. For many years he was on the governing council of the mortgage and finance division of the NAREB and was

president of the successor to this committee, the National Mortgage Board. He has been a member of MBA since 1937.

C. ARMEL NUTTER

C. Armel Nutter is the new Eastern representative on the Board. He is a native of Delaware and went to its state university to take electrical engineering, later transferring to business administration. He took his degree there and was captain of the football team. He took military training in college and this June completed 15 years' service as second lieutenant in the Officers Reserve Corp.

He was associated with the Bell Telephone Company after graduation and later as manager of a law office. In 1931 he and his brother established a mortgage and real estate company in Camden, the Nutter Mortgage Service, and he is the firm's president and treasurer. The firm represents about eight banks in appraisals and property management as well as several life insurance companies.

Mr. Nutter is vice president of the New Jersey Association of Real Estate Boards, a director of the Camden Chamber of Commerce and a past president of the Camden County Real Estate Board.

ALLYN R. CLINE OF HOUSTON

Allyn R. Cline is a native of Houston and attended the schools there. He went to work for the Houston Land and Trust Company in 1907 and remained with this institution until 1929. He served as secretary, treasurer, vice president, trust officer and director during this time, which also included a period of war service. He then went to the San Jacinto Trust Company as vice president, was later made executive vice president and still later president of the San Jacinto National Bank. In 1934 he resigned to head the Cline Mortgage and Trust Company, of which he is now president.

He was admitted to the Texas Bar in 1916. He has served as head of the Trust Section of the Texas Bankers Association and has been vice president

ALLYN R. CLINE

for Texas of the ABA. He is a past president of the Texas Mortgage Bankers Association and a director of Gulf Bitulithic Company, Universal Land Company, Texas MBA and Mortgage Loan Association of Houston.

At the stag dinner: Past President A. D. Fraser of Cleveland is concentrating on the shrimp cocktail while Secretary George H. Patterson's attention has been attracted elsewhere.

At the Board of Governors dinner: Two Board members and a past president have something in common. Left to right: A. D. Wilson of Denver, Past President W. Walter Williams of Seattle and C. W. Mead of Omaha.

DO MORTGAGE LENDERS GROW OLD BEFORE THEIR TIME?

If They Do, This Author Says He Knows the Reason Why.

By MARK A. STRANG

FOR a quarter of a century I have been lending money on real estate security and trying to get it back. During that time I have learned some things not to do in the mortgage business. But the experiences of one lifetime are pitifully inadequate as dependable data. Hence the need for research. During the last five years remarkable progress has been made, due to the awakening of mortgage lenders to the vital necessity for organized studies and recordation of experiences.

How long is the remaining economic life of a dwelling? Upon what basis can it be predicted? Mortgage lenders do not know; yet an estimate of it has to be made when a twenty or twenty-five year loan is being considered. Possibly research will develop the answer.

In rental income properties it is pretty generally recognized that value does not exceed the net income capitalized. What is the net income? It is surprising how little is known on this subject from recorded experience. A thorough study of the subject would be justified if dependable data were developed from which reasonably accurate predictions of the ratio of expense to income could be made. A cursory survey was recently made which resulted in one sound conclusion; namely, that the pausity of recorded experience in connection with buildings containing four or less family units is appalling.

What is the rate of decline in a residential neighborhood? About all we know is that it does decline. But that is some progress for only a few years ago people bought both vacant and improved residential lots on the assumption that they would increase in value. The rate of decline must be predicted in order to estimate the certainty, quality and duration of the stream of benefits to flow from ownership of a property in the neighborhood. How else could a long term mortgage be intelligently patterned? It is still necessary to guess. We call it judgment. The object of all research is to narrow the range within which judgment must be exercised.

Not only lenders but also builders, brokers and home buyers should have some source of dependable information on the market. There is need for research to solve the problem of measuring statistically the home building and home financing market. Why is it that home building booms in this country have occurred during periods of prosperity while in Europe home building has been much more rapid in periods of depression? These and many other problems are crying for solution.

WHAT do we REALLY know about home building, about the home financing market? How much economic life remains for any given building? How fast do neighborhoods decline? What causes the violent fluctuations in the building cycle? Why have building booms in the U. S. occurred in prosperous periods while in Europe it is just the reverse? You may think you know the answers to these and the many other questions that very vitally affect mortgage lending today—but do you have the data on which you can cite a scientific opinion? That is the theme of this article: That this business of mortgage lending is supported by woefully little scientific data—data which have been compiled from careful research and study. The author is Chief Underwriter of the FHA in San Francisco and recently spoke at the Stanford University Business Conference.

A glimpse at FHA's method of attack may be interesting and surely will emphasize the necessity for research in property financing. The National Housing Act was passed at a time when the real estate financing structure of the country was in a state of collapse. It was not the purpose of the Act to afford relief to distressed borrowers nor to bail out lending institutions at Government expense. The purpose was and is to create and maintain a sound structure for mortgage loans on residential property and to improve housing standards. The vehicle adopted by means of which to accomplish these purposes is a system of mutual mortgage insurance. No Government money was made available for these loans. Private lending institutions had to be induced to lend on mortgage security in the residential field, notwithstanding their disastrous experiences immediately preceding the passage of the Act. Obviously a sound structure had to be devised if loans were to be made. Although few reliable data were available intensive research soon led to the conviction that short-term low-percentage loans coupled with second mortgages at exorbitant rates, the prevailing system before FHA, cannot withstand a major depression; while long-term amortization loans of sufficiently high ratio of loan to value to obviate the necessity of secondary financing, fair much better under adverse economic conditions.

Although relatively little experience had been recorded in this latter type of loan, sufficient reliable data were found to warrant the pioneers in making this basic assumption upon which FHA proceeded to its present position of dominance in the field of housing finance: Long-term high-percentage amortization loans are adequately secured if made on good property in good locations and to borrowers who are themselves good risks.

Whenever a loan is made, risk is created, and it is the function of the Underwriting Division of FHA to measure that risk in every mortgage offered for insurance. For this purpose a risk rating system has been devised and is constantly being refined and improved as a result of widespread intensive research and the development within this and other governmental and private agencies of reliable data upon which sound conclusions can be based.

In developing this risk rating system some old widely accepted concepts have been exploded and some interesting and enlightening ones have been evolved. Different mortgages vary as to degree of risk, and it is fallacious to presume that they fall into merely two classes: safe ones and unsafe ones. Mortgage risk is an entity, a measurement of which can be expressed in simple terms. The overall degree of mortgage risk is composed of all the possibilities of trou-

ble, expense and loss. The elements of risk include difficulty and expense in connection with collections, excessive servicing costs, delay and cost of foreclosure, cost of rehabilitation and carrying until sold, and cost of resale, as well as loss, if any, on resale.

Many Complex Factors Govern Mortgage Risk

The factors contributing to mortgage risk are numerous, complex and subject to an almost infinite number of possible combinations in practical cases. To segregate, classify and weigh these factors accurately enough to obtain correct results in practical application was the task facing FHA at the outset because the Act requires that mortgages insured be grouped according to risk characteristics. In the light of all available data a large number of experienced mortgage men under the leadership of Frederick M. Babcock, Director of the Underwriting Division of FHA, set up a system of measuring mortgage risk and giving it numerical expression. A great mass of statistics has been compiled from over five hundred thousand mortgages, the risk characteristics of which have been measured by this system. Constant study of these statistics brings to light any inherent weaknesses in the system and any faulty or inaccurate application of it in the field.

It is not presumed even now after several years of application of the system that the relative importance of the various factors has been determined with the ultimate degree of accuracy. Future research and experience will lead to further refinements.

In connection with amenity income dwellings, that is, properties salable to buyers interested in the direct services of the property rather than possible monetary income, there are twenty-four significant factors, contributing to mortgage risk. They are:

Relationships:

- Ratio of Loan to Value
- Ratio of Total Payment to Rental Value
- Ratio of Life of Mortgage to Economic Life of Building

Property:

- Structural Soundness
- Resistance to Elements
- Resistance to Use
- Livability and Functional Plan
- Mechanical and Convenience Equipment
- Natural Light and Ventilation
- Architectural Attractiveness
- Degree of Conformity or Non Conformity

Location:

- Relative Economic Stability
- Protection from Adverse Influences
- Freedom from Special Hazards
- Adequacy of Civic, Social and Commercial Centers
- Adequacy of Transportation
- Sufficiency of Utilities and Conveniences
- Level of Taxes and Special Assessments
- Appeal

Borrower:

- Social and Economic Characteristics
- Motivation in Relation to Transaction
- Employability and Earning Stability
- Relation of Obligations to Transaction
- Relation of Income to Transaction

The relative importance assigned to these factors is indicated by weights in figures appearing in FHA forms which are used throughout the country in processing applications for mortgage insurance.

When good judgment is exercised in recording the degree of risk attributable to each of these features in a given case, a mortgage pattern is formed which clearly indicates and measures the overall risk in the mortgage transaction.

The system is not a formula which can be applied without discrimination. It requires the exercise of good judgment at every step. Qualified Architects, Valuators and Credit Examiners are employed and constantly trained by experienced mortgage men. They are subjected to a rigid written examination once a year. Dependable data are being gathered and recorded constantly. For instance, with each Valuator's Report a data sheet is turned in giving rents asked and received, listing and sale prices of comparable properties in the immediate neighborhood and other significant facts such as typical family income level, percentage of owner occupancy and percentage of homes vacant. These data are recorded in a file on the outlined neighborhood and are available at all times to Valuators who are assigned cases in the area as well as to the Review Offices and Section Chiefs.

Past Is the Only Guide To the Mortgage Future

Value does not exist unless future benefits are in prospect. Mortgage risk lies in the future. All estimates of the future are hypothetical. Appraisal procedure is the estimating of probabilities. Assumptions are embodied in all appraisals and estimates of mortgage risk. We have no means of judging the future except by the past.

These are some of the reasons why exhaustive research and discriminating application of data is necessary in property financing.

An examination of one feature of mortgage risk, Relative Economic Stability, will illustrate the value and necessity of reliable data to guide the judgment of individuals passing on mortgage loans. The rating assigned to this feature, Relative Economic Stability, is an estimate of the probable continuing marketability of the subject property attributable to its site, *as effected by* the financial capacities and financial attitudes of owners, occupants, and prospective purchasers, and as related to similar estimates of all residential properties in the Economic Background Area, irrespective of competitive characteristics. A maximum weight of 40 points has been ascribed to this feature out of a possible 100 points in the Rating of Location.

"Economic Background Area" Must Be Understood

To rate this feature intelligently it is necessary first to determine the rating of the Economic Background Area within which the subject property lies as compared with other economic background areas. This requires examination of data on factors which create cities and influence the extent, character and direction of city growth. These data are found in (a) statistics dealing with the volume, trend, and composition of population, (b) compilations relating to the cyclical fluctuations, trends, and diversifications of industrial employment, and the cyclical fluctuations and trends of commercial and specialty employment, (c) information pertaining to natural resources, social and cultural advantages, business conditions, and legislative policies, and (d) facts concerning geographical, meteorological and topographical characteristics of the area. It is then necessary to gather and examine information pertinent to the economic structure of the area under consideration. This material embraces (a) the nature and history of the principal economic activities prevalent in the area under consideration, (b) the nature, size and stability of industrial and commercial activities within the area, (c) population trends, including rate of growth and racial, age and family distribution, (d) natural resources, and (e) miscellaneous items such as type of tenure prevalent in the community, distribution of incomes, taxation policies and schools and cultural institutions.

Sources of Economic Background data are: Chambers of Commerce, Real Estate Boards, Industrial Bureaus, Industrial Corporations, Employment Agencies, Financial Institutions, Utility Companies, Clearing House Associations, Educational Institutions, Labor Organizations, Agricultural Agents,

Publications of U. S. Chamber of Commerce, Publications of City, County and State Governments, and Bureaus of Vital Statistics.

Then Determine "Relative Economic Stability" Point

After a rating of the Economic Background has been established it becomes possible to rate the feature under consideration—Relative Economic Stability. This rating is intended to reflect the degree to which the occupants of properties in the vicinity of the subject location participate in the general advantages attributed to the Economic Background Area. To be significant the rating must be based upon a comparison with all other neighborhoods in the area both competitive and noncompetitive. The elements to be investigated and considered in rating this feature of mortgage risk are:

- Stability of Family Income.
- Sufficiency of Family Income.
- Social Characteristics of Neighborhood Occupants.
- Stage and Trend of Neighborhood Development.
- Probability of Forced Sales and Foreclosures.

The fact is well established that mortgage risk varies with the group income characteristics of the occupants of properties in the immediate neighborhood.

At the bottom of the employment scale are those working in the capacity of laborers. The next group is composed of semi-skilled mechanics and lower-grade clerks. Further up the scale are mechanics and office workers. Next are foremen and chief clerks. Above this group are junior executives. It is considered that this group presents, for the purpose of determining mortgage risk, the best income characteristics in the entire employment field. At the top of the employment scale is found the senior executive group. Experience has demonstrated that although their leadership is most firmly established, the stability of incomes is not as great as that evidenced in the junior executive class, therefore, the feature Relative Economic Stability is rated lower in a neighborhood occupied by senior executives than in a neighborhood occupied by junior executives.

After the degree of stability of family incomes in the neighborhood is determined the sufficiency of that income must be investigated. If it is found that the neighborhood occupants as a group have bought properties too expensive for their incomes the rating will be affected adversely. The social characteristics of the neighborhood occupants including moral qualities, habits, abilities, social, educational and cultural backgrounds must be ascertained. They indicate the group attitude toward obligations and living standards which affect mortgage risk and must be reflected to some degree in the rating of Relative Economic Stability. The stage and trend of neighborhood development indicates the degree of need for housing which has important bearing on mortgage risk. In newer neighborhoods, consideration should be given to (a) the physical need or shortage of homes of the type and in the price class contemplated, (b) whether the need originates with a financially capable group of purchasers, and (c) whether the sales prices and values approximate cost of completed properties. In older, built-up neighborhoods the principal consideration will be given to the presence of a ready financially capable market for the homes which exist in the neighborhood, at their current value levels. The findings here, are also reflected in the rating of Relative Economic Stability.

Points to Low Rate of FHA's Losses So Far

The probability of forced sales and foreclosures due to unwise control of expenditures which sometimes appears as a group characteristic in neighborhoods is of utmost importance. The financial condition of the occupancy group must be determined. For example, there is greater risk of foreclosure in residential areas where mortgages represent a high ratio of loans to values, than in an area where the average mortgage indebtedness is a low percentage of values. The added burden of interest and amortization payments on the larger loans may be such that during trying times foreclosure becomes almost inevitable. For this reason when properties in a neighborhood are heavily mortgaged, an element of instability may be introduced. Mortgage risk is greater in such neighborhoods and the degree of risk must be reflected in the rating of Relative Economic Stability.

All this to rate intelligently one of the twenty-four features of mortgage risk, indicates the volume of research necessary in a program of sound housing finance. The wisdom of it is being demonstrated daily. Bankers and mortgage men of the old school shook their heads in grave concern when it was proposed to insure 80 and 90 percent mortgages; yet of 363,906 mortgages insured nationally over a period of four years up to January 1, 1939, only 946, about ¼ of one percent, have been foreclosed and of these only 435, or about one-eighth of one percent, were transferred to FHA.

Declares There Is a Vital Need for More Research

The risks involved in mortgage investment lie in the future. The process of measuring mortgage risk is the estimating of probabilities. Such forecasting to merit the confidence of the investing public and lending institutions must be based upon thorough knowledge of past events in the field of property finance and that means research in the fullest sense of the word resulting in data, facts verified, recorded, analyzed, classified and judiciously weighted and applied with discrimination.

To avoid bogging down in a morass of vaguely related data, unsystematically collected and analyzed, it is necessary to develop a sound practical method of appraisal and then proceed to secure only those data which are necessary to make it work, and to plan a program for their assembly and analysis.

Only residential properties of specified types are embraced in the FHA program. Therefore its research necessarily confined within fairly narrow limits. A clearcut understandable statistical record of every case is recorded from which generalizations can be made with greater and greater assurance as the multitude of examined cases mounts. The whole process of statistical procedure is to enable generalization out of specific experience and items.

I believe nearly every Valuator possessed of that necessary quality, a skeptical and inquiring mind, yet blessed with enough good sound horse sense to keep his feet on the ground has at some time in his experience toyed with the concept that net rental income from a desirable residential property capitalized should be its value. Yet records of the past and daily experience demonstrates that they do not move in the market at that price. They bring more.

FHA has thrown the light of research on this concept and presented it in new and interesting form capable of practical application in property finance. Dependable generalizations from the statistics recorded are:

Where the market motive is largely dollar income, the net rental income

(Turn to the back page please)

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BYRON T. SHUTZ........ *President*
DEAN R. HILL........ *Vice President*
GEORGE H. PATTERSON........ *Secretary-Treasurer*

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MORTGAGE TREND

The savings and loans led in mortgage recordings in August with 33 percent of the total, followed by banks with 23 percent. The former made $112,516,000 and the latter $80,049,000. Next come "individuals" with $58,826,000, or 17 percent, and "others" with $49,549,000, or 14 percent. Insurance companies accounted for 9 percent of the total and mutual savings banks for 4 percent. These figures are from the Federal Home Loan Bank Board survey which showed $345,580,000 of home mortgages made in August. August recordings were nearly sixteen million above those of July which is contrary to the usual seasonal decline, the Board says. In the first eight months of this year nearly 2½ billion dollars of home mortgages have been recorded in the United States as shown in this survey. Members who would like individual figures for a state should write the headquarters office.

* * *

Urban residential construction will reach a nine-year peak this year—its first billion dollar year since 1930, the FHLBB says. This compares with $779,802,800 last year.

STRANG ON RESEARCH

(*Continued from page 8*)

groups? What is the typical family income of a neighborhood?

However, I believe we *have* found the answer to one question. Why do mortgage lenders grow old prematurely? *Because they have to make important decisions daily without adequate data.*

A Governors table at the Stag: Left to right: J. P. Hogan of New Orleans, Frank J. Mills of Ft. Wayne, Claude A. Campbell of Toledo, Charles A. Mullenix of Cleveland and R. O. Deming, Jr. of Oswego, Kan.

At the general session on the first day: President S. M. Waters introduces Dr. William G. Murray of Iowa State College who spoke on the influences of the present European War on American farm values. This address attracted considerable comment, particularly from institutional members and farm lenders.

Three past presidents of MBA at the stag dinner: W. Walter Williams of Seattle, Sylvanus B. Nye of Buffalo, New York, and H. S. Cody of Winston-Salem, N. C. The stag dinner, always one of the most popular entertainment features of MBA conventions, was a sell-out affair at the Book-Cadillac.

Around the Convention: H. G. McCall of the H. G. McCall Co. of Minneapolis, Chas. A. Mullenix of The Cuyahoga Estates, Inc., of Cleveland, J. W. McClaren of the Berkshire Life Insurance Co. of Pittsfield, Mass., and C. J. Claassen of the Farmers National Co. of Omaha.

capitalized is the value. Where the market motive is largely direct services of the property, that is owner occupancy, the value is more than the net rental value capitalized. How much more depends upon the amenities of home ownership present, and these are capable of measurement and expression in dollars. The amenities in dollars added to the gross monthly rental income and the total capitalized, is the value.

As a matter of fact this method of valuation elaborated is being utilized by the Administration. In practical application the monthly amenity increment is ascertained by studying cases in which valuations have already been established. In this study the various conditions entering into the valuation and justifying it must be known and available for analysis. The factors vary for properties in different value groups and for properties exerting various degrees of owner-occupancy appeal. Thus, within any one value group, the higher amenity increment percentages are found to relate to properties of higher owner-occupancy appeal. With regard to properties in different value groups, the higher percentages relate to the properties in the higher value groups, assuming equal degrees of owner-occupancy appeal.

"A Dwelling Is Worth 100 Times the Monthly Rent"

The method of capitalization employed in amenity income properties is unlike that in general use in connection with rental income properties. It is in a sense a scientific adaptation of the old rule of thumb—"a dwelling is worth 100 times the monthly rent." The ratio of the total amount of the value to the monthly amount of the returns including the amenity increment is found to be relatively high or low depending upon the certainty, quality and probable duration of the returns in the future. This ratio is used as a conversion factor. The conversion factor is, in any given case, equal to the value of the property divided by the derived monthly value. It may be used to determine the derived monthly value figure when the value of the property is known or to ascertain an estimate of value of the property when the derived monthly value is known.

High ratings of Location and Property when combined with long remaining economic life estimates indicate high conversion factors. To illustrate: The rental value of a dwelling to a tenant is found by comparison to be $45.00 a month; however, its location and other characteristics exert strong owner-occupancy appeal. Typical owner occupants of such a property obtain returns which include independence in use and control, satisfaction and pride from the mere fact of ownership and enhanced social status. This monthly amenity increment is found to be $5.00 a month in this case. We have therefore a derived monthly value of $50.00. It is found that the ratings of Location and Property are high and estimate of remaining economic life is relatively long. Therefore a conversion factor of 105 is justified. Multiply $50.00, the derived monthly income, by 105 and you have an estimate of value of $5250. This figure is tested by the market price of comparable properties and subjected to the substitution concept before it is accepted as the value estimate for the purpose of mortgage insurance.

"Value" Can Be Defined in Many Different Ways

There are many purposes for which valuations are made, and there are, of necessity, many possible definitions of "value." Definition depends upon the purpose for which the estimate is to be used. FHA has only one objective in view in connection with valuation. It therefore utilizes only one concept of value. The word "value", as used by the Administration, refers to the price which a purchaser is warranted in paying for a property for continued use or as a long-term investment. This concept is defined as the price which well-informed typical buyers, acting intelligently, voluntarily, and without necessity, would pay for the property. It always presumes a price which is justified by the future owner. This definition of value describes the exchange value concept and places emphasis on the idea that value is a price which typical buyers are warranted in paying. This is presumed to be equivalent to the price a typical owner is justified in paying, whether he is actually a new purchaser or the present owner. A primary distinction is made between value, as here defined, and market price. Both are value concepts and take cognizance of a market, either present or implied. There are cases where the two may be identical in amount, but quanitative differences are frequently encountered. Another way of describing this is to distinguish between what a property is worth and what the current market thinks it is worth.

The valuation of dwelling properties for the purpose of determining the amount of collateral is required under the National Housing Act, but it solves only a part of the mortgage lending problem. Valuation is never an end in itself. There are two ways in which property value constitutes security for a loan. The first, and by far the most important one, is the incentive to make interest and principal payments on the loan because of the importance of the property to the owner. The second is the value of the property recoverable under conditions of foreclosure. Mortgages should be set up not only to avoid loss on resale of the property after foreclosure, but also to avoid, in a high degree, the probability of foreclosure. As frequently happens a borrower sets out to buy a $10,000 home which fairly appraises at $10,000 and applies for an $8,000 loan. He may have a splendid credit record and all the attributes of a good borrower except that his income indicates reasonable ability to pay on a $4,000 loan only. Notwithstanding security against loss under foreclosure a prudent lender should not make such a loan, and FHA would not insure it.

Observes That the FHA Has Awakened Interest in Research

One of the most important contributions to research in property financing made by FHA is, I believe, the awakening of bankers and other mortgage lenders to the importance of research. Largely as a result of this activity in close contact with lending institutions the responsible executives have become data minded, and more and more they are demanding not only the conclusions of their appraisers and other subordinates but also the facts upon which the conclusions are based. A good beginning has been made, but there is a long way yet to go. The field of research in property financing is teeming with possibilities and is attracting some of the best minds in the country.

The history of property finance is characterized by collapse after collapse and that history will probably go on repeating itself until we find, through research, the answers to more of the vital questions necessary to guide the judgment of those responsible for the investment of mortgage funds.

What is the percentage of owner-occupancy appeal in a neighborhood?

How long is the remaining economic life of a dwelling? What is the rate of decline of a neighborhood? What causes the violent fluctuations in the building cycle? How can decent housing be provided and financed for the lower income

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